87-974

No.

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1987

PARLOR FURNITURE OF HICKORY, INC.,
Petitioner,
v.
BURLIN B. MILLER
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE NORTH CAROLINA COURT OF APPEALS

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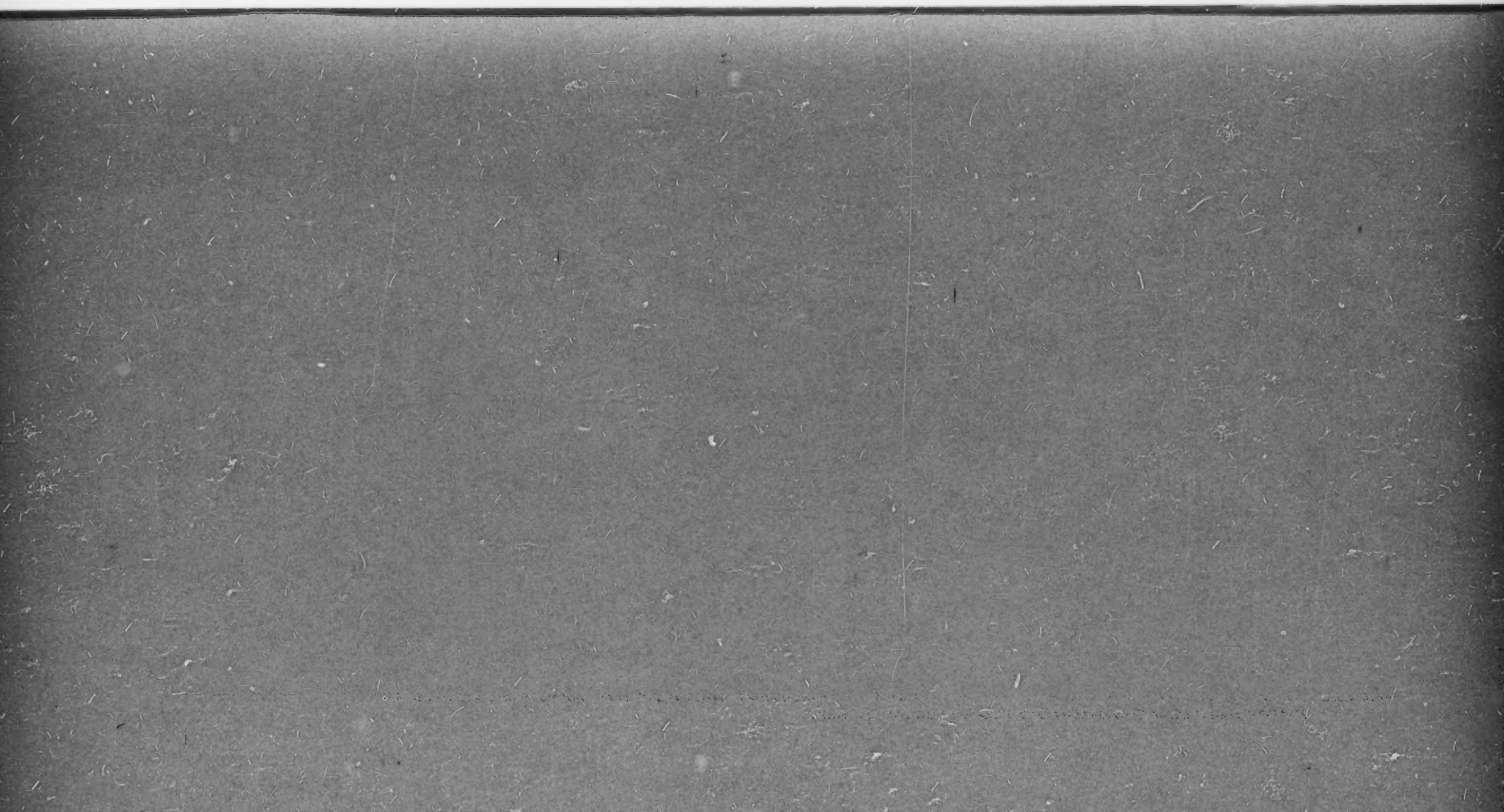

QUESTION PRESENTED FOR REVIEW

Whether the North Carolina common law of contracts, which would otherwise permit the respondents to terminate the lease of the petitioner, is preempted by the United States Bankruptcy Code, 11 *U.S.C.S.* § 365(e)(1) (Law. Co-op. 1985), even though the petitioner currently has no petition or case pending in the bankruptcy court?

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REASONS FOR DENYING THE WRIT

This case involves nothing more than the power of a North Carolina landlord to terminate the lease of a tenant pursuant to a so-called "ipso facto" clause entitling the landlord to terminate in the event that the tenant filed a petition in bankruptcy. In this case, the petitioner, Parlor Furniture of Hickory, Inc. (hereinafter referred to as Parlor Furniture), filed a petition in bankruptcy sometime in March 1983 which petition was dismissed by the bankruptcy court on February 19, 1985 (App. to Petition at A-13 - A-14). The lease between Parlor Furniture and respondent Burlin B. Miller and Georgia B. Miller (hereinafter referred to as the Millers),[1] specifically empowered the Millers as the lessors to terminate the lease if Parlor Furniture petitioned to be or was adjudicated to be bankrupt (*Id.* at A-13). Such provisions are enforceable under North Carolina common law. *See Carson v. Imperial '400' National, Inc.*, 267 N.C. 229, 147 S.E.2d 898 (1966). Nine days after Parlor Furniture's petition in bankruptcy was dismissed, the Millers filed a Complaint in Summary Ejectment seeking to end the lease on the basis of the ipso facto clause. The trial court held that the eviction was barred by 11 *U.S.C.S.* § 365(e)(1) (Law. Co-op. 1985). The North Carolina Court of Appeals reversed the trial court and remanded the case on the ground that § 365(e)(1) was not applicable because the petition in bankruptcy had been dismissed (*Id.* at A-4 - A-10). That ruling is the basis for Parlor Furniture's petition for a writ of certiorari.

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[1]The lease was executed by respondent Burlin B. Miller and his wife Georgia B. Miller. Mrs. Miller is not named as a respondent because she died during the course of the proceedings below.

Section 365(e)(1) of the Bankruptcy Code provides in pertinent part:

> Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on –
>
> (B) the commencement of a case under this title. . . .

Prior to the enactment of this section, ipso facto clauses had been enforceable under § 70(b) of the former Bankruptcy Act. The legislative history to § 365 shows that it was enacted because of the adverse impact of ipso facto clauses upon the administration of the bankrupt's estate. As was stated in H.R. Rep. No. 95-595 to accompany H.R. Rep. No. 8200, 95th Cong., 1st Sess. (1977):

> Subsection (e) invalidates ipso factor [facto] or bankruptcy clauses. These clauses, protected under present law, automatically terminate the contract or lease, or permit the other contracting party to terminate the contract or lease, in the event of bankruptcy. This frequently hampers rehabilitation efforts. If the trustee may assume or assign the contract under the limitations imposed by the remainder of the section, then the con-

> tract or lease may be utilized to assist in the debtor's rehabilitation or liquidation.

(Reprinted at 11 *U.S.C.S.* § 365(e)(1).) That § 365(e)(1) was enacted in response to the adverse effects of ipso facto clauses on the administration of the bankrupt's estate was expressly recognized in *In re National Shoes, Inc.*, 20 B.R. 55, 57 (Bankr. S.D.N.Y. 1982). Moreover, the legislative history to § 365(e)(1) indicates that the ipso facto clause in question in a given case is not "invalidated in toto, but merely made inapplicable *during the case* for the purposes of disporition [disposition] of the executory contract or unexpired lease." H.R. Rep. No. 95-595, *supra* (emphasis added). Clearly, the focus of the statute is to assist the administration of the estate and nothing more. Hence, if the administration of an estate is not affected or involved, there is no reason to apply the statute.

That is precisely the case here. Parlor Furniture's petition in bankruptcy was dismissed. The obvious purpose of ipso facto clauses is to give the lessor protection if it appears, through specified and significant indicia, that the lessee is or may soon become financially unable to perform. *Cf. Uniform Commercial Code* § 2-609; *N.C. Gen. Stat.* § 25-2-609 (1985) ("When reasonable grounds for insecurity arise with respect to the performance of either party the other may in writing demand adequate assurance of due performance and until he receives such assurance may if commercially reasonable suspend any performance for which he has not already received the agreed return"). Parlor Furniture impliedly suggests that 11 *U.S.C.S.* § 365 was intended to ignore these legitimate interests of lessors. Such is not the case.

> The unenforceability of ipso facto or bankruptcy clauses proposed under this section will require the courts to be sensi-

> tive to the rights of the nondebtor party to executory contracts and unexpired leases. If the trustee is to assume a contract or lease, the courts will have to insure that the trustee's performance under the contract or lease gives the other contracting party the full benefit of his bargain.

H.R. Rep. No. 95-595, *supra*. Given the sensitivity that should be paid to the interests of lessors under the statute, there is no conceivable reason why North Carolina law should be preempted where there is no federal interest under the Bankruptcy Code to vindicate. Indeed, in light of the sensitivity that Congress intended the courts to pay to the interests of lessors, applying § 365(e)(1) where no federal interest is implicated would be contrary to the intention of Congress.

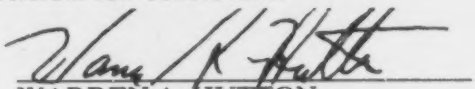
That the true issue presented here is one of preemption is beyond dispute. *See Allied Technology, Inc. v. R.B. Brunemann & Sons, Inc.*, 25 B.R. 484, 496 (Bankr. S.D. Ohio 1982) (because ipso facto clause was unenforceable, debtor's act of assumption cured the default, "a curing which is preemptive of any relevant state law"). Indeed, even though the term preemption is not used by Parlor Furniture in its petition, its reference to "the supremacy of acts of congress [sic] when enacting laws regarding bankruptcy" (Petition at 14) and its citation of *U.S. Const.* art. I, § 8 (Petition at 3) leave no doubt that the instant case is one involving the doctrine of preemption.

The courts have long recognized that, while the federal bankruptcy laws do preempt state law, they do so only where the state law conflicts with the federal law. *See, e.g., Stellwagen v. Clum*, 245 U.S. 605 (1918); *Hayden v. McDonald*, 719 F.2d 266, 273 (8th Cir. 1983) (citing cases). This view is, of course, consistent with the doctrine of

preemption as generally applied. *See, e.g., Rose v. Arkansas State Police*, 107 S. Ct. 334 (1986). Preemption of state law, morever, is not to be lightly presumed. *California Federal Savings & Loan Association v. Guerra*, 107 S. Ct. 683 (1987). In the instant case, Parlor Furniture has offered no reason to presume that state law ought to be preempted. Parlor Furniture simply relies on the "plain language" of § 365(e)(1) and the complaint that the North Carolina Court of Appeals improperly "carved out an exception" to the statute (Petition at 13-15). In fact, the North Carolina Court of Appeals merely recognized that the purposes behind the enactment of § 365(e)(1) were of no relevance to the present case. This is evident from the legislative history of the statute and the cases which have interpreted it. Inasmuch as preemption is not to be lightly presumed and inasmuch as § 365(e)(1) was not intended to apply to the instant situation, the Millers contend that the North Carolina Court of Appeals properly analyzed the issues in this case. Hence, there is no need for this Court to hear the case because no federal question is even presented. The question here should be treated as being solely a matter of North Carolina common law which, in this case, is of no interest to the federal courts because it in no way impairs federal policy.

CONCLUSION

For the reasons specified in the foregoing brief, the respondent, Burlin B. Miller, respectfully requests the Court to deny the petition for certiorari.



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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing document was served on the opposing attorney of record:

Curt J. Vaught
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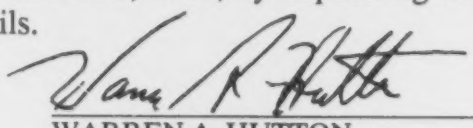
this 31st day of December, 1987, by depositing same in the United States Mails.



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